

EXCEPTION ORIGINAL



BEFORE THE ARIZONA CORPORATION COMMISSION

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COMMISSIONERS

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2005 MAR 25 P 12:13

AZ CORP COMMISSION
DOCUMENT CONTROL

IN THE MATTER OF QWEST CORPORATION'S
FILING OF RENEWED PRICE REGULATION
PLAN

DOCKET NO. T-01051B-03-0454

IN THE MATTER OF THE INVESTIGATION OF
THE COST OF TELECOMMUNICATIONS ACCESS

DOCKET NO. T-00000A-00-0672

Arizona Corporation Commission

DOCKETED

MAR 25 2005

STAFF'S EXCEPTIONS TO THE RECOMMENDED OPINION AND ORDER

I. Introduction

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On March 16, 2005, the Arizona Corporation Commission Hearing Division issued its Recommended Opinion and Order on Qwest Corporation's ("Qwest's") Emergency Motion to Suspend the Inflation Minus Productivity Factor Adjustment. The Staff files the following Exceptions to the Recommended Opinion and Order ("ROO").

II. Suspension of the April 1, 2005 Adjustment Does Not Violate Scates or Constitute Retroactive Ratemaking

Staff supported Qwest's motion to suspend the April 1, 2005 adjustment until the end of this proceeding, as long as the consolidated appeals by Qwest of Decision Nos. 66772 and 67047 were suspended for a like period of time. The ROO rejects this approach and contains two alternative options for Qwest. The first option would require Qwest to make the adjustment effective April 1, 2005. The second option would allow Qwest to defer the adjustment as long as it deposits the amount of any reduction in an interest bearing escrow account so that ratepayers will receive the full benefit of the reduction when final rates are set. These options are intended to address concerns that to do otherwise, the Commission may be violating *Scates*¹, and ultimately the rule against retroactive

¹ *Scates v. Arizona Corporation Commission*, 118 Ariz. 531, 578 P.2d 612 (App. 1978).

1 ratemaking. Staff does not believe that suspension of the adjustment by itself would violate either
2 *Scates* or the rule against retroactive ratemaking.

3 In *Scates*, the Court found that the Commission could not change rates absent a fair value
4 finding. Staff does not believe that a mere suspension of the April 1, 2005 adjustment, alone would
5 violate *Scates*, because a suspension does not change rates, it merely delays collection. If, on the
6 other hand, the Commission decided to simply terminate the adjustment, that may violate *Scates*.
7 Staff believes that there is an important distinction between suspension of the adjustment versus
8 termination of the adjustment, as far as *Scates* is concerned.

9 One of the leading cases on retroactive ratemaking is *Arizona Grocery Co. v. Atchison, Topeka*
10 *& Santa Fe Railway, Co.*, 284 U.S. 370 (1932). The following excerpt from the Court's decision
11 provides a good description of the conduct that is prohibited under this principle:

12 Where the Commission has, upon complaint and after hearing, declared what
13 is the maximum reasonable rate to be charged by a carrier, it may not at a later
14 time, and upon the same or additional evidence as to the fact situation existing
15 when its previous order was promulgated, by declaring its own finding as to
reasonableness erroneous, subject a carrier which conformed thereto to the
payment of reparation measured by what the Commission now holds it should
have decided in the earlier proceeding to be a reasonable rate.²

16 In Staff's opinion, a suspension of the April 1, 2005 inflation/productivity adjustment by itself
17 does not constitute retroactive ratemaking. The Commission by suspending the adjustment for a
18 limited period of time would not be declaring its earlier finding or order to be unreasonable and
19 would not be instituting any new rates that would have retroactive impact. The Commission would
20 merely be holding the adjustment in abeyance until a final order is issued, as long as the consolidated
21 appeals are suspended for a like period.

22 If Qwest chooses the second option, the ROO requires that any settlement account for the full
23 value of the adjustment (including the time value of money). If the parties, on the other hand, are
24 unsuccessful in their efforts to settle the various issues arising from this case, then the ROO requires
25 that Qwest provide ratepayers the benefit of the reduction through the escrow account. While the
26 Commission certainly can resolve all of these issues at this time, Staff believes the Commission can
27

28 ² *Arizona Grocery*, 284 U.S. at 390.

1 also choose to address the issues surrounding any ultimate reduction when the suspension period
2 ends, or when final rates are approved. Not addressing all of these issues at this time may provide the
3 Commission with more flexibility to determine the appropriate result at the time that final rates are
4 approved in this Docket.

5 Staff agrees with the Administrative Law Judge ("ALJ") that under the Commission's Orders
6 interpreting the Price Cap Plan, a liability accrues on April 1, 2005, under the Continuation Clause
7 until the Commission enters an Order terminating the Plan or approving a new or modified Plan. This
8 would have to be considered in any comprehensive settlement as would the consolidated appeals,
9 which are related to this issue.

10 In summary, Staff believes that the Commission can suspend the April 1, 2005
11 inflation/productivity adjustment without running afoul of either *Scates* or the retroactive ratemaking
12 rule. It is not necessary for the Commission to address all of the issues surrounding the April 1, 2005
13 adjustment at this time. Rather, the Commission could wait until the time final rates are established
14 to address these issues. If the Commission agrees with this position, the language attached as Exhibit
15 1 may be helpful.

16 **III. The Proposed Escrow Account May Be Difficult to Accomplish Given the Uncertainties**
17 **Surrounding Settlement Discussions**

18 Option 2 under the ROO requires the Company to deposit the "amount of the reduction" in an
19 interest bearing account, with the intention that ratepayers receive the full benefit of the reduction
20 when final rates are set. Staff believes that while well intentioned, the purpose of the proposed escrow
21 account and how it would operate is not clear. Further, it would be very difficult to determine "the
22 amount of reduction" before the case concludes. The amount of the reduction will be dependent upon
23 the length of settlement discussions as well as the length of time it takes to process the case in
24 general. Thus, attempting to determine the amount of the reduction at this stage of the proceeding
25 with any accuracy would be extremely difficult if not impossible.

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1 **IV. The ROO May Lead to the Result Wherein the Commission Is Forced to Continue to**
2 **Litigate the Consolidated Appeal, Even Though a Settlement Is Reached on All of the**
3 **Other Issues Arising from this Case.**

4 Qwest agreed to suspend the consolidated appeals if the April 1, 2005 reduction was
5 suspended pending the outcome of the settlement discussions in this case. Qwest, the Commission
6 and RUCO stipulated to suspension of the pending appeals while settlement negotiations were
7 ongoing.

8 Staff has always believed that any settlement of this case should be a comprehensive
9 settlement and as such should resolve the issues raised in the pending appeals. A far less optimal
10 result would be obtained if the parties were to settle all of the other issues in this case except the
11 appeals, despite the fact that the appeals could have a major impact on the ultimate rates charged
12 customers under the price cap plan. Further, if the appeals go forward independent of the settlement,
13 this will, in Staff's opinion, make settlement much more difficult because of the uncertainty created
14 by the pending appeals.

15 There is a strong possibility that the ROO may have the unintended effect of encouraging
16 Qwest to ask the Court to move forward with the appeals since under the two options presented the
17 Company will either have to make the adjustment or set the money aside in an account for
18 distribution at a later date. As with any appeal, there are risks associated with going forward before
19 the Court. There is always the risk that the Court may not accept the Commission's or RUCO's
20 position in the appeal. The Commission should ultimately structure its Order so that it does not have
21 the unintended effect of encouraging yet more litigation on this issue. Staff believes that suspension
22 of the April 1, 2005 adjustment at this time, with resolution of other related issues accomplished in
23 the Commission's order approving final rates in this case, would ensure the Commission maximum
24 flexibility, and encourage a comprehensive settlement of the issues, rather than piecemeal resolution
25 of the issues and further litigation.

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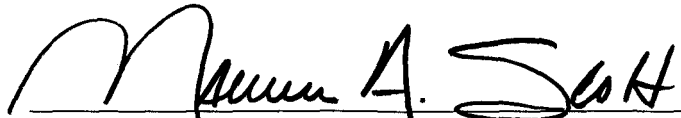
28 ...

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1 **V. Conclusion**

2 Staff does not believe that suspension of the April 1, 2005 adjustment by itself violates *Scates*
3 or constitutes retroactive ratemaking. Staff recommends modifications to the Recommended Opinion
4 and Order as discussed herein.

5 RESPECTFULLY submitted this 25rd day of March, 2005.

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25 Copy of the foregoing mailed this
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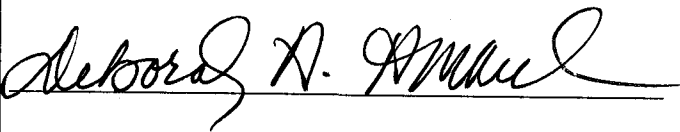
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Exhibit "1"

Page 5, DELETE lines 15 through 28, Page 6, DELETE lines 1 through 13.

Page 5, INSERT the following at line 15:

We agree with RUCO that based on the terms of the current Price Cap Plan, and our holdings in Decision Nos. 66772 and 67047 that unless we approve a new Plan or terminate the current Plan, Qwest is required under the Continuation Clause of the Plan to make the April 1, 2005 productivity adjustment. However, the Commission certainly has the discretion to suspend the April 1, 2005 reduction, to accommodate comprehensive settlement discussions in this case. We do not believe that a mere suspension of the April 1, 2005 reduction would violate Scates¹, or the principle that the Commission can not modify rates absent a fair value finding. We are not terminating the April 1, 2005 adjustment. The liability associated with the April 1, 2005 adjustment will continue to accrue. We will address the accrued liability for the April 1, 2005 adjustment in the final rate order in this Docket.

We also do not believe that suspension of the April 1, 2005, reduction is by itself retroactive ratemaking. The Commission by suspending the adjustment is not declaring its earlier finding or order to be unreasonable and is not instituting any new rates with retroactive impact.

We can also see that adjusting rates for basic services downward now, and then adjusting them again in the opposite direction in the near future as a result of final rates being set in the Renewed Plan, could cause consumer confusion. Therefore, we believe that a suspension of the adjustment is appropriate.

Our Decision granting Qwest's Motion is motivated solely by a desire to avoid consumer confusion and to accommodate comprehensive settlement discussions in this case. Qwest's claim that it is under-earning under traditional rate of return analysis has no bearing on our Decision. That is an issue to be determined through the evidentiary hearing process. Further, in no way does our

¹ *Scates v. Arizona Corporation Commission*, 118 Ariz. 531, 578 P.2d 612 (App. 1978).

conclusion indicate one way or the other how the Commission will decide the issue of whether there should be a productivity adjustment when we consider Qwest's Renewed Plan currently before us.

Page 7, lines 26-27, MODIFY Finding of Fact 15 by deleting "obligation to make" and insert in its place "liability relating to".

Page 8, INSERT new Finding of Fact 17 to read as follows:

A suspension of the April 1, 2005 productivity /inflation adjustment is appropriate to allow for comprehensive settlement discussions between the parties and avoid customer confusion.

Page 8, RENUMBER old Finding of Fact 17 to new Finding of Fact 18.

Page 8, DELETE old Finding of Fact 18 and INSERT in its place as Finding of Fact 19:

It is in the public interest to allow Qwest to suspend the implementation of the April 1, 2005 productivity adjustment until final rates are set in this docket, as long as the consolidated appeals are suspended for a similar time period, at which time the Commission will address issues surrounding the April 1, 2005 adjustment.

Page 8, DELETE old Finding of Fact 19.

Page 8, DELETE old Finding of Fact 20.

Page 8, DELETE Conclusion of Law 3 and INSERT in its place:

Pursuant to Arizona Constitution Article 15, Section 14, the Commission must determine the fair value of a utility's property before modifying its rates. Suspension of the April 1 2005 adjustment by itself does not constitute a change in rates but merely delays collection, and therefore, does not violate *Scates*.

Page 8, DELETE Conclusion of Law 4 and INSERT in its place:

Suspending the April 1, 2005 productivity adjustment by itself does not violate the prohibition on retroactive ratemaking.

Page 9, MODIFY Conclusion of Law 5 to read:

It is in the public interest to grant Qwest's Motion to suspend the April 1, 2005 productivity adjustment to the extent discussed herein and for the reasons set forth herein.

Page 9, DELETE Conclusion of Law 6.

Page 9, MODIFY the first Ordering Paragraph as follows:

IT IS THEREFORE ORDERED that Qwest Corporation's Emergency Motion to Suspend the Productivity Adjustment to Basket 1 required on April 1, 2005, is granted to the extent discussed herein and for the reasons set forth herein.

Page 9, DELETE the second Ordering Paragraph.